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THE ADMINISTRATION'S PROPOSED MILLENNIUM FUND — WHILE SIGNIFICANT — WOULD LIFT FOREIGN AID TO JUST 0.13 PERCENT OF GDP

by Isaac Shapiro and David Weiner¹

Over the past week the Bush Administration has announced a new initiative on foreign aid, most recently indicating that it plans to increase such spending by \$10 billion over the three-year period from 2004 through 2006. This short analysis examines how the resulting levels of aid would compare with historic levels. It also lays out some of the policy questions and implications raised by the President's proposal, an assessment that should be considered preliminary as many of the details of the proposal have yet to be clarified or determined. The analysis builds off an earlier analysis by our two organizations which found that under the Administration's budget for 2003, the share of the economy dedicated to foreign economic aid would be at its second lowest level in the post-World War II era and the share of government spending dedicated to foreign economic aid would tie for its lowest level in this period.²

President Bush's proposed increase for foreign economic aid would result in the sharpest increase in aid spending in decades. This proposal and his strong speech underscoring the importance of foreign economic aid represent a potential turning point in the aid debate.

On the other hand, the proposed increase for the Millennium Fund would not begin to take effect until 2004 and would not take full effect until 2006, thereby requiring several years of Congressional assent and continued Presidential support. Further, the resulting level of spending on foreign economic aid would rise to only 0.13 percent of the economy or Gross Domestic Product in 2006, still below — and compared with most years, well below — the share of GDP the United States contributed in any year from 1946 to 1995. The United States would continue to contribute a far smaller portion of its economy to aid than nearly every other donor country. In addition, the share of the budget that the United States would devote to aid would still be lower than in almost any year from the end of World War II through the mid-1990s.

How Much of an Increase, and How Aid Would Compare with Previous Levels

The definition of foreign economic aid used here includes the budget category called "International Development and Humanitarian Assistance" as well as the "Economic Support

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² Isaac Shapiro and Nancy Birdsall, "How Does the Proposed Level of Foreign Economic Aid under the Bush Budget Compare with Historical Levels?," Center on Budget and Policy Priorities and Center for Global Development, revised March 20, 2002.

Fund.” As explained in the Appendix, if this approach errs, it does so on the side of being too expansive a definition of foreign economic aid to poor countries.

The Administration has proposed creating a new “Millennium Challenge Account” funded through increases in foreign economic aid that total \$10 billion over the three years starting in 2004.³ This analysis assumes that for the years 2004, 2005, and 2006, the Administration would add \$1.67 billion, \$3.34 billion, and \$5 billion respectively to what the Administration has already proposed for those years. (It is unclear whether the Administration is proposing a \$5 billion increase for 2006 relative to what the Administration proposes to spend for 2003 or what it previously proposed to spend for 2006. By assuming the latter, this analysis may err on the side of projecting a somewhat larger increase than the Administration may actually support.)

The Administration’s proposed increases would require Congressional approval in each of the next three years. If approved by Congress, this proposal, once it had been fully phased in, would represent a sizeable increase in foreign economic aid spending, to a total of \$16 billion in 2006. Aid would jump by 38 percent over the 2003 level, after adjusting for the effects of inflation. (The Bush Administration is saying it would increase aid by 50 percent, from \$10 billion currently to \$15 billion in 2006. The Administration shows a larger percentage increase both because it does not take into account the effects of inflation and because it uses a lower figure for current aid. The lower base means that any dollar increase in spending yields a relatively larger increase in percentage terms.)

As a share of the economy and the budget, however, foreign economic aid would still be below its share in nearly every year between the end of World War II and the mid-1990s. Under the Administration’s proposal:

- *Aid as a share of the economy.* Foreign economic aid spending would constitute 0.13 percent of the economy (or GDP) in 2006, an increase from its current level of 0.11 percent, but still below its share of the economy in every year from the end of World War II through 1995. Aid as a share of the economy would still be far below its average of 0.20 percent during the 1980s, and even further below its average during the latter half of the 1940s, as well as the 1950s, 1960s, and 1970s.

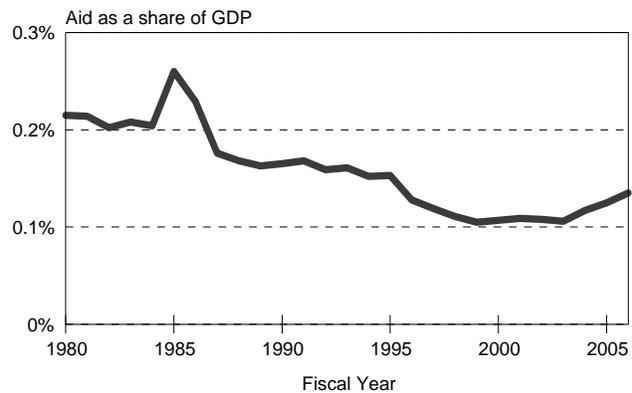
Aid as a share of the economy is the yardstick that is typically used for international comparisons. If the United States devotes 0.13 percent of its economy to aid in 2006, this share would still be much lower than the share of the economy — 0.31 percent — now contributed by the typical or median donor

³ This is the level of the proposed increase as of March 19. When originally proposing the increase March 14, the Administration said it would increase aid by \$5 billion over three years.

country to development assistance.⁴ The United States would lift its share to the current share of Italy, but in all likelihood the other 20 “donor countries” would still contribute a larger share of their economies to aid than the United States would. (Even though European countries already contribute a much larger share of their economies to aid than the United States does, the European Union also recently pledged to increase aid levels significantly in its countries over the next few years.)

Foreign Economic Aid Trends 1980-2006

(Figures for 2003-2006 are the levels proposed by Bush Administration)



- Aid as a share of the budget. Foreign economic aid spending would equal 0.73 percent of the federal budget in 2006, which would be a higher share of the budget than in 1992, 1994, and every year from 1996 onward, but would be a lower share of the budget than in any other year since the end of World War II. So in 2006, aid would be a lower share of the budget than it was in the entire period from 1946-1991 (and lower than in 1993 and 1995 as well) and would remain significantly below its average level of 0.92 percent during the 1980s.

Table 1
Spending on Foreign Economic Aid

	1980s Average	In 2006 under Administration's Proposal	Comment on 2006 Figures
As a share of the economy	0.20%	0.13%	Lower than from 1946-1995
As a share of the budget	0.92%	0.73%	Lower than from 1946-1991

Source: Center on Budget and Policy Priorities analysis of data from the Office of Management and Budget, the Congressional Budget Office, and U.S. AID.

⁴ The Organisation for Economic Co-operation and Development, *2001 Development Co-operation Report*, March 19, 2002.

Table 2 includes annual figures from 1962 through 2006 on actual and proposed foreign economic aid spending, based on the Office of Management and Budget and Congressional Budget Office data. For the years from 1946 to 1961, this paper relies on data from U.S. AID.⁵

Some Questions Concerning the New Approach

Some elements of the Administration's proposal have yet to be announced, and many others will only be determined through further discussions within the Administration and by Congressional action. Until further details emerge from the policy process, the most authoritative descriptions of the Administration's plans remain the text of the President's March 14 speech announcing the proposal and several brief Administration fact sheets. Any assessment of the policy implications should thus be considered preliminary.

In his speech the President proposed what he called a "new compact for development," in which "greater contributions from developed nations must be linked to greater responsibility from developing nations." To carry out the United States' part of this proposed bargain, the President promised to increase U.S. aid "above and beyond" the amount requested in his current budget, and to put these additional funds in the new "Millennium Challenge Account."

According to the President, funds from the Millennium Account will support a variety of different development objectives, including expanding efforts to combat AIDS, increasing access to information technology, helping developing country firms sell products in foreign markets, strengthening education and training, and enhancing agricultural productivity.

Three broad standards will guide U.S. decisions on whether countries receive support from the new fund: whether they are "ruling justly, investing in their people, and encouraging economic freedom." According to the President, adherence to these standards will be measured by the extent to which countries have adopted policies designed to reduce corruption, protect human rights, promote the rule of law, improve education and health care, open their markets, pursue sound fiscal policies, and reduce bureaucratic obstacles to entrepreneurship.

As the earlier part of this analysis documents, the increased aid expenditures proposed by the President would reverse a long-term trend of declining aid budgets. If approved, the proposed aid increases have the potential to enhance substantially the reach and the effectiveness

⁵ Based on the U.S. AID data, U.S. "Economic Assistance" (the category AID uses that is somewhat analogous to the definition of foreign economic aid this paper uses) averaged 1.75 percent of GDP from 1946 to 1948. From 1949 to 1952, it averaged 1.53 percent of GDP, while from 1953 to 1961, it averaged 0.60 percent of GDP.

The same pattern applies when foreign economic aid is measured as a percentage of all federal outlays. According to the U.S. AID data, Economic Assistance averaged 10.45 percent of all federal outlays from 1946 to 1948. From 1949 to 1952, it averaged 9.58 percent of outlays and from 1953 to 1961, it averaged 3.31 percent of outlays.

of U.S. development assistance programs. A boost in the United States aid budget would also create pressure for other major aid donors to increase their aid expenditures by comparable amounts. The Administration's proposal to link aid to measurable performance in developing countries will, in principle, be welcomed by many in the U.S. development policy community, members of Congress, and other aid donors.

The President's speech and efforts by Administration officials to explain his proposal have raised many critical policy questions. Answers to some of these questions await further Administration clarification and discussions among the Executive Branch, Congress, and non-governmental stakeholders. But the questions underscore just how difficult it will be to fulfill the promise of the President's new proposal:

- What criteria will be used to measure the performance of developing countries? How will these criteria be devised? Who will make the decisions?

U.S. and other development policymakers have tried for several decades to develop criteria to guide decisions on worthy aid recipients. Much of value can be drawn from this experience, but the mixed success of past efforts to be more "selective" in the distribution of aid highlights the scale of the challenge facing the Administration.

- How will the U.S. aid program reach people living in countries that are not determined to be "good performers"?

Will people with the misfortune to be living under corrupt or inept governments benefit from the new aid resources in the Millennium Fund?

- What will happen to the regular U.S. development assistance budget once the Millennium Challenge Account is created, and how much money will flow into that budget?

If funds in the Millennium Account are reserved for development projects in "good performers," will there be pressure from within and from outside the Administration to shift other assistance funds to strategically important but politically and economically poor-performing countries? Will the Administration's requests for development assistance funds outside of the Millennium Account decrease as additional funds are steered into the Millennium Account?

- What if a larger-than-expected number of countries qualify for assistance from the Millennium Account: will budget contributions to the fund increase?

As the President's proposal begins to take shape, the role of Congress will come to the fore. Will Congress approve the President's budget requests for the Millennium Account? How might Congress seek to modify the proposal? Congressional approval of aid increases on this

scale cannot be taken for granted. In addition, given the size of the proposed increases and the policy conditions proposed by the President, it is likely that Congress will want a significant hand in shaping key elements of the proposal. Will Congress accept the policy conditions proposed by the President for determining eligibility for funds in the new aid account? Will it seek to write other conditions into law? Will Congress seek to earmark large amounts of the new funds for favored programs? Will funding earmarks be supported by non-governmental development organizations that have become increasingly influential politically and have come to play critical roles in disbursing U.S. development assistance funds?

In short, without a doubt, both in scope and approach the President's proposal is a noteworthy one. Even if adopted in full, however, it would not return aid levels as a share of the economy and the budget to historical levels and would leave the United States lagging behind the level of commitments made by other countries. A more comprehensive assessment of the new approach awaits further details on the plan, as well as answers to the questions laid out in this analysis.

Table 2 Foreign Economic Aid Trends, 1962-2006

Fiscal Year	Aid in 2003 Dollars (outlays in billions)	Aid as a Percent of GDP	Aid as a Percent of Budget Outlays
1962	\$17.3	0.576%	3.06%
1963	\$16.5	0.526%	2.83%
1964	\$15.9	0.480%	2.60%
1965	\$15.7	0.448%	2.61%
1966	\$17.2	0.457%	2.56%
1967	\$16.5	0.418%	2.16%
1968	\$13.5	0.329%	1.61%
1969	\$11.8	0.274%	1.42%
1970	\$10.7	0.244%	1.27%
1971	\$9.8	0.220%	1.13%
1972	\$11.5	0.245%	1.26%
1973	\$10.3	0.205%	1.09%
1974	\$9.0	0.176%	0.94%
1975	\$10.9	0.218%	1.03%
1976	\$10.0	0.191%	0.89%
1977	\$11.5	0.208%	1.00%
1978	\$12.8	0.220%	1.06%
1979	\$12.2	0.201%	1.00%
1980	\$12.8	0.215%	0.99%
1981	\$13.0	0.214%	0.97%
1982	\$12.1	0.202%	0.88%
1983	\$12.7	0.208%	0.88%
1984	\$13.4	0.204%	0.92%
1985	\$17.7	0.260%	1.14%
1986	\$16.3	0.229%	1.02%
1987	\$12.9	0.176%	0.82%
1988	\$12.7	0.168%	0.79%
1989	\$12.8	0.163%	0.77%
1990	\$13.1	0.165%	0.76%
1991	\$13.2	0.168%	0.75%
1992	\$12.8	0.159%	0.71%
1993	\$13.3	0.161%	0.75%
1994	\$13.0	0.152%	0.72%
1995	\$13.5	0.153%	0.74%
1996	\$11.6	0.128%	0.63%
1997	\$11.2	0.119%	0.61%
1998	\$10.9	0.111%	0.59%
1999	\$10.7	0.105%	0.56%
2000	\$11.2	0.107%	0.58%
2001	\$11.5	0.109%	0.59%
2002*	\$11.5	0.108%	0.55%
2003*	\$11.6	0.106%	0.55%
2004*	\$13.2	0.117%	0.62%
2005*	\$14.5	0.125%	0.67%
2006*	\$16.0	0.135%	0.73%

*Data for 2002 through 2006 are Congressional Budget Office estimates of the Administration's budget proposal plus assumed effects of the Millennium Challenge Account. Figures are adjusted for inflation based on the CPI-URS from 1962-2000 and CBO's inflation projections for 2001 onwards.

Source: Author's analysis of Office of Management and Budget and CBO data.

Appendix

Foreign economic aid can be defined and measured in a number of ways. The definition used here — which is the same definition the Center on Budget and Policy Priorities used in papers released in 2000 and 2001 on this subject — includes the budget category called "International Development and Humanitarian Assistance" (subfunction 151) as well as the "Economic Support Fund" (which is part of subfunction 152). The focus here is on discretionary spending in these areas.⁶

- International Development and Humanitarian Assistance includes funding for areas such as bilateral development aid, assistance to countries in transition (mainly those that once were part of the former Soviet Union), certain contributions to multilateral institutions that can be used for development purposes, the Child Survival and Disease Program, humanitarian aid, emergency relief, migration and refugee assistance, and efforts to combat the drug trade. Some of the activities funded by this part of the budget have purposes other than helping strengthen the economies of the world's poor countries and reducing poverty. For this reason, some analysts do not consider all of the funds spent under this budget category as "development aid."
- The Economic Support Fund consists of economic assistance the United States provides to other countries (such as Israel and Egypt) based on considerations of special economic, political, or security needs and United States interests. Not all these funds are targeted on development. Still, since some of the ESF funds that countries receive do promote economic development, this paper errs on the side of an inclusive definition and counts ESF funds in its analysis.

By including *all* the spending in the International Development and Humanitarian Assistance category as well as the Economic Support Fund, the figures used here somewhat overstate the amount of United States aid designed to combat poverty and its effects in the world's poor countries.

⁶ More specifically, the definition of foreign economic aid used here includes *discretionary* or annually appropriated spending. *Mandatory* spending in these areas consists primarily of inflows of funds into credit liquidating accounts. This cash flow is a result of loans made before 1992, when the Credit Reform Act went into effect; it does not affect the current level of credit assistance and thus is ignored in this analysis.